# Q4FY10 & FY10 Result Update

May 20, 2010

NTPC's principal business is generation and sale of bulk power. Other business includes providing consultancy, project management and supervision, oil and gas exploration and coal mining. The total installed capacity of the company as of 31 March 2010 was 31,704 MW as against 30,144 MW at then end of FY09. 1,490 MW of capacity was declared commercial during the year (incl 500 MW under JVs) as against a target of 3,300 MW. NTPC disappointed on the capex addition front in FY10.

NTPC, India's largest power generator came out with its Q4FY10 results. Results were below expectations due to some one off adjustments. Net sales from power generation were up 7.9% y-o-y and 10.4% q-o-q due to higher generation and benefits of capacity addition carried out in FY09 and part of FY10. Operating margins improved to 21.6% in Q4FY10 vs 19.4% in Q4FY09 due to lower fuel costs. However, q-o-q margins fell from 30.1% in Q3FY10 due to prior period sale adjustments and provision for employee costs. Employee costs increased by 30.3% q-o-q. Q4FY10 PAT fell by 4.5% y-o-y and 14.7% q-o-q to Rs. 2,017.7 cr.

On a full year basis, NTPC's gross generation increased 5.75% to 218.84 bn units. This exceeded the MoU excellent target of 217 bn units. NTPC contributed 28.6% of total electricity generated in the country in FY10. It reported total sales of Rs. 46,322.6 cr, up 10.5% y-o-y, operating margins of 26.8% vs 24.8% in FY09 and a PAT of Rs. 8,728.2 cr, up 6.4% y-o-y. Lower growth in PAT despite higher operating margin was mainly due to lower other income and higher tax outgo.

## Key Highlights of the Results

| Income Statement | Q4FY10 | Q4FY09 | % Chg y-o-y | Q3FY10 | % Chg q-o-q | FY10 | FY09 | % Chg y-o-y |
|---|---|---|---|---|---|---|---|---|
| Generation | 12305.3 | 11404.9 | 7.9% | 11149.2 | 10.4% | 46168.7 | 41791.2 | 10.5% |
| Others | 48.1 | 40.9 | 17.6% | 34.5 | 39.3% | 153.9 | 132.5 | 16.1% |
| **Total Sales** | **12353.4** | **11445.8** | **7.9%** | **11183.7** | **10.5%** | **46322.6** | **41923.7** | **10.5%** |
| Other income | 627.7 | 1009.1 | -37.8% | 779.1 | -19.4% | 2924.1 | 3322.5 | -12.0% |
| Total Income | 12981.0 | 12454.8 | 4.2% | 11962.9 | 8.5% | 49246.7 | 45246.2 | 8.8% |
| Fuel Cost | 8346.0 | 8015.8 | 4.1% | 6767.3 | 23.3% | 29462.7 | 27110.7 | 8.7% |
| Employee Cost | 745.6 | 620.3 | 20.2% | 572.3 | 30.3% | 2412.4 | 2463.1 | -2.1% |
| Total Operating Expenditure | 9687.7 | 9225.9 | 5.0% | 7818.5 | 23.9% | 33902.2 | 31525.9 | 7.5% |
| EBITDA | 3293.4 | 3228.9 | 2.0% | 4144.4 | -20.5% | 15344.5 | 13720.3 | 11.8% |
| **Margins w/o OI %** | **21.6** | **19.4** | | **30.1** | | **26.8** | **24.8** | |
| Interest | 481.8 | 540.4 | -10.8% | 341.8 | 41.0% | 1808.9 | 1996.2 | -9.4% |
| Depreciation & Non cash charges | 732.2 | 726.4 | 0.8% | 661.4 | 10.7% | 2650.1 | 2364.5 | 12.1% |
| PBT before prior period items | 2079.4 | 1962.1 | 6.0% | 3141.2 | -33.8% | 10885.5 | 9359.6 | 16.3% |
| Taxation | 61.8 | -151.2 | 140.9% | 776.3 | -92.0% | 2157.3 | 1158.2 | 86.3% |
| **Net Profit** | **2017.7** | **2113.4** | **-4.5%** | **2365.0** | **-14.7%** | **8728.2** | **8201.4** | **6.4%** |
| EPS | 2.4 | 2.6 | -4.5% | 2.9 | -14.7% | 10.6 | 9.9 | 6.4% |

(**Source:** Company, HDFC Sec)

- NTPC reported generation revenues of Rs. 12,305.3 cr in Q4FY10, up 7.9% y-o-y and 10.5% q-o-q. Generation increased by 2.6% y-o-y and 7.5% q-o-q to 58.36 bn units. For FY10, NTPC reported a topline from generation of Rs. 46,168.7 cr, up 10.5% y-o-y while generation in terms of number of units was up 5.75% to 218.84 bn units. This was driven by capacities added in FY09, the full benefit of which can be seen in FY10, part benefit of capacities added in FY10 and higher PLF recorded by gas plants. We highlight that NTPC earnings contain recurring prior period revenues on account annual review of tariff orders by the regulator, which have been discussed below.

| PLF | Q4FY10 | Q4FY09 | FY10 | FY09 |
|---|---|---|---|---|
| Coal | 97.5 | 97.7 | 90.8 | 91.1 |
| Gas | 83.3 | 73.9 | 78.4 | 67.0 |

(**Source:** Company, HDFC Sec)

- There are a number of adjustments carried out by the company due to regulatory / other reasons which have impacted performance and are highlighted below:
  1. Adjustment for prior period sales - Full-year sales contain negative Rs. 600.6 cr pertaining to previous years which has been recognized based on the orders issued by the CERC/ATE. This is in comparison to positive Rs. 1,020 cr adjusted in FY09. As a result, sales are lower to that extent.
  2. Adjustment for tax recoverable from customers and deferred tax - Full year sales includes (-) Rs. 719.93 cr (previous year Rs. 758.3 cr on account of income tax recoverable from customers as per CERC Regulations, 2004 and Rs. 248.5 cr (previous year Nil) on account of deferred tax recoverable from customers as per CERC Regulations, 2009.

3. Tax expense for prior period - Provision for current tax for the year is net of tax related to earlier years amounting to Rs. 525.4 cr (previous year Rs.1395.31 cr). The net increase during the year in the deferred tax liability is Rs. 209.1 cr (previous year decrease Rs. 448.84 cr) has been debited to Profit & Loss Account.
4. Provision for employee expense - NTPC also increased provisions for employee expenses that are pending finalization of pay revision. Based on the guidelines issued by Department of Public Enterprises (DPE), Government of India (GOI) the pay revision of the executive category of employees has been approved during the year. Pending finalisation of pay revision in respect of employees in the non-executive category, provision of Rs. 314.5 cr and Rs. 858.95 cr (previous year Rs. 0.18 cr and Rs. 344.5 cr) has been made for the year and upto year respectively on an estimated basis having regard to the guidelines issued by DPE.

- Other income and other operating income have fallen by 37.8% y-o-y and 19.4% q-o-q to Rs. 627.7 cr. On a full year basis, other income and other operating income is lower by 12% at Rs. 2,924.1 cr. This has been mainly due to lower interest income with maturing of government bonds held by the company. These bonds, issued in 2003-04 for settlement of past dues of state electricity boards, are regarded as an important milestone in the turnaround of the company and the sector. At the end of FY10, the company had a cash balance of Rs. 14,459.5 cr as against Rs. 16,271.6 cr at the end of FY09, down 11.1% y-o-y.

- Operating margins increased to 21.6% from 19.1% in Q4FY09 and fell from 30.1% in Q3FY10. In FY10, the margins are at 26.8% as against 24.8% in FY09. On a y-o-y basis, margins expanded in Q4FY10 due to lower fuel costs and a fall in other expenses, which was partly offset by a rise in employee costs. On a q-o-q basis the operating margins were impacted due to a rise in fuel and employee costs and lower revenue due to adjustment of prior period sales. NTPC made a provision towards pay revision of employees of Rs. 128 cr in Q4FY10 as against Rs. 60 cr in Q3FY10. Given below is the operational expenditure breakup for the quarter.

| Cost | As a % of sale in Q4FY10 | As a % of sale in Q4FY09 | As a % of sale in Q3FY10 | As a % of sale in FY10 | As a % of sale in FY09 |
|---|---|---|---|---|---|
| Fuel cost | 67.6 | 70.0 | 60.5 | 63.6 | 64.7 |
| Employee cost | 6.0 | 5.4 | 5.1 | 5.2 | 5.9 |
| Others | 4.8 | 5.2 | 4.3 | 4.4 | 4.7 |

(Source: Company, HDFC Sec)

- Interest cost decreased by 10.8% y-o-y but increased 41% q-o-q to Rs. 481.8 cr in Q4FY10. For the full year, interest costs were down 9.4% at Rs. 1,808.9 cr. Depreciation for the quarter was flat y-o-y and up 10.7% q-o-q in Q4FY10. For FY10, depreciation was up 12.1% y-o-y at Rs. 2,650.1 cr, in line with the capex capitalized by the company.

- PAT decreased by 4.5% y-o-y and 14.7% q-o-q to Rs. 2017.7 cr despite higher topline and expansion in operating margins due to the various adjustments at the sales and tax level carried out by the company. Also, lower other income led to lower bottomline growth. On a full year basis, the company reported a PAT of Rs. 8,728.2 cr, up 6.4% y-o-y. EPS stood at Rs. 10.6.

- NTPC declared a total dividend (including interim dividend) of Rs. 3.8 per share for FY10 as against Rs. 3.6 in FY09.

## Other Developments

**Delay in capacity addition, misses target for FY10**

The total installed capacity of the company as of 31 March 2010 was 31,704 MW as against 30,144 MW at then end of FY09. 1,490 MW of capacity was declared commercial during the year (incl 500 MW under JVs) as against a target of 3,300 MW. 1,560 MW of capacity was added during the year. NTPC once again disappointed on the capex addition front in FY10. Presently, NTPC has 17,830 MW under construction at 17 locations. Details of the capacities added during the year have been summarized in the table given below.

| Project / Unit | Capacity (MW) |
|---|---|
| **NTPC Owned** | |
| Kahalgaon Stage II | 500 |
| Dadri – Stage II Unit 5 | 490 |
| **Under JVs** | |
| RGPPL – Block 1 | 640 |
| Less on account of overall de-rating of RGPPL | - 180 |
| Kanti Stage 1 | 110* |
| **Total** | **1,560** |

* capacity stabilized during the year (Source: Company, HDFC Sec)

Details of the capacities that were declared commercial during the year have been summarized in the table given below.

| Project / Unit | Capacity (MW) | Commercial Operation Date |
|---|---|---|
| Kahalgaon Unit #7 | 500 | 22.03.2010 |
| Dadri Unit #5 | 490 | 31.01.2010 |
| Bhilai Unit #2 | 250 | 21.10.2009 |
| Bhilai Unit #1 | 250 | 22.04.2009 |
| **Total** | **1,490** | |

(Source: Company, HDFC Sec)

NTPC incurred a capex of Rs. 101 bn in FY10 against a guidance of Rs. 177 bn, signaling likely slippages in execution of projects. It has cited delay in bulk tendering as a reason for missing the targets for capex spend. NTPC has guided for capacity addition of 4,150 MW and capex outlay of Rs. 223 bn for FY11E. The guidance for capacity addition in FY11E is weak and raises concerns regarding NTPC's ability to achieve the targeted 50 GW capacity by the end of the current five-year plan. In terms of capacity addition underperformance may continue for FY11. Out of a target of 22.4 GW in the XI Plan (FY08–12), NTPC has commissioned 4.3 GW over FY08-10. Targets in the XII Plan are expected to be bigger at 28GW, and the company expects to place 34GW of orders over the next 1.5 years. BHEL doubling capacity to 20GW and the setting up of manufacturing facilities by other private sector players could mean that capacity addition could be better going ahead. Given below are the projects that are expected to come on stream in FY11.

| Project / Unit | Capacity (MW) |
|---|---|
| Sipat Stage 1, Unit 1 | 660 |
| Jhajjar, Unit 1 & 2 | 1,000 |
| Korba Stage III, Unit 7 | 500 |
| NCTPP Stage II, Unit 6 | 490 |
| Simhadri, Stage II, Unit 3 & 4 | 1,000 |
| Farakka, Stage III, Unit 6 | 500 |
| **Total** | **4,150** |

(Source: Company, HDFC Sec)

**Bulk tendering**

NTPC expects to launch the second phase of bulk tendering for super critical boilers, which will include 8 units. Additionally, the company also plans to bid out certain 500MW units for extensions to certain plants such as the ones in Singrauli and Vindhyanchal. However, the company is likely to continue its policy of restricting the bids to Indian manufacturers.

**Focus on Renewables**

By 2017, NTPC plans to have at least 1000 MW through renewable energy resources such as wind, hydro, solar, biomass and geo-thermal.

**Few hiccups along the way**

Hydro projects – Very little clarity emerged on the status of the three hydro projects being developed by the company. While NTPC expects the projects to be completed by the eleventh plan period, we do not see the projects being commissioned in the near future. Further, the company has stated that fixed assets, capital work-in-progress and construction stores and advances include Rs. 676.5 cr in respect of one of the hydro power project, the construction of which has been suspended temporarily from May 18, 2009 on the advice of the Ministry of Power, GOI. Presently, the Issue regarding resumption of the project is under consideration with the GOI. Pending decision, borrowing costs of Rs. 23.7 cr have not been capitalised from the date of suspension.

Secondly, the company is executing a thermal power project in respect of which possession certificates for 1,489 acres of land has been handed over to the company and all statutory and environment clearances for the project have been received. Subsequently, a high power committee has been constituted as per the directions of GOI to explore alienate location of the project since present location is stated to be a coal bearing area. Aggregate cost incurred up to March 31, 2010 Rs. 183.1 cr is included in Fixed Assets. The management is confident of recovery of cost incurred, hence no provision is considered necessary.

**Augmenting fuel security**

NTPC has taken a number of measures to ensure and improve fuel security. This includes:

- Model Coal Supply Agreement signed with Coal India Ltd (CIL) for supply of coal to NTPC stations for 20 years.
- Developing captive coal mines in India. NTPC is working on captive coal mines with target of 47 MTPA by 2017 from the 6 blocks allotted. More than 6,735 acres of Land in Pakri Barwadih and about 1,594 acres of land in Chatti Bariatu coal block have been acquired. Land acquisition for Dulanga and Talaipalli are in progress. Rehabilitation Action Plan (RAP) has been approved by NTPC Board for Pakri Barwadih, Chatti Bariatu and Kerandari. Mining Plan approved for Dulanga (7 MTPA) and Talaipalli (18 MTPA).
- JV agreement has been signed with CIL for development, operation and maintenance of Coal Blocks and Integrated Power Projects
- Pursuing acquisitions abroad. Due diligence for acquisition of stakes in two coal mines in Indonesia is under progress and a consultant is appointed for carrying out due diligence for one coal block in Mozambique. I
- International Coal Ventures Ltd (ICVL) has been incorporated on 20.05.2009 as a JV company of NTPC, RINL, SAIL, NMDC and CIL for sourcing coking and thermal coal from overseas countries like Australia, Mozambique, Canada, Indonesia and USA. ICVL is pursuing 3 thermal coal opportunities in Indonesia, Australia and South Africa
- NTPC has placed an order for import of 12.5 MMT of coal to meet the short term deficit.
- Tying up long term gas supply with GAIL. In FY10, gas supplies increased to 13.88 MMSCMD (up 29% over previous year).
- NTPC has entered into a long term contract for supply of RLNG of 2.0 MMSCMD on firm basis and 0.5 MMSCMD on fallback basis signed with GAIL for 10 years.
- Pursuing E&P for gas.
- Under NELP VIII, NTPC has been allotted one block at Cambay basin as a sole operator and three blocks as a member of consortiums.

## Concerns

Fuel related - NTPC's operations depend on timely availability of fuel. NTPC's gas-based plants were hampered by poor fuel supply in the earlier part of FY09, resulting in sub-optimal capacity utilization. Moreover, if coal supplies do not grow in line with capacity additions then it could affect the PLF of the coal-based plants. However, given the current energy supply scenario this risk seems to be mitigated for the time being. Delay in the outcome of the RIL-RNRL gas dispute could delay NTPC's capex plans. Also, as mentioned above transportation bottlenecks could adversely impact the availability of coal and thereby impact NTPC's operations adversely.

Technology - NTPC is implementing larger modules and newer technologies such as 660 MW and 800 MW super critical technology and alternative fuels such as gas and hydro more aggressively, which could place demands on its project management and technology absorption skills.

Project execution - Delays in commissioning of new capacities remains a key concern

## Conclusion

NTPC is a leader in the power segment. However, the stock as well as the company has performed below market expectations over the past year. The main areas of concern include timely supply of equipment, execution of capex plans and availability of fuel. Also, till date, NTPC has not won a single UMPP based on competitive bidding. This is a cause of concern as the power sector gradually shifts platform to a more open bidding system. The management indicated that it is implementing systems and processes to enable it to operate effectively post January 2011 era when competitive bidding for projects will be the norm.

The near-term outlook for the company remains subdued. The PLF of its coal-based plants has come down from 92.5% in FY09 to 91.4% in FY10 due to forced outages. While another way to boost the topline would be faster commissioning of newer projects, the progress on this count is also limited, with 1,490 MW of capacity addition during the year, against an original targeted capacity addition of 3,300 MW. Further, actual expenditure on projects during FY10 has been 43% lower than planned, indicating a slower-than-expected progress of the on-going projects. In all, 17,800 MW of projects are under various stages of construction, which would increase its total capacity by more than half in the next 2-3 years.

While there has been a significant improvement in the availability of gas, the impact on aggregate financials is limited, as gas-based plants account for only a little over one-tenth of total capacity. The PLF of gas-based plants has gone up from 67% in FY09 to 78.4% in FY10 and can go up further on the back of expected supplies in FY11. Next, NTPC has signed a MoU with Secretary (Power), Government of India for generating 224 billion units of electricity during the financial year FY11, an increase of only 2.4% y-o-y compared to the 218.8 bn achieved in FY10.

NTPC is trading at about 2.4x its FY11 (E) BV of Rs. 83. Historically, NTPC has traded at a premium to its peers due to stable cash flow, the regulated model that enables it to pass on fuel costs and interest rate, strong balance sheet, and strong parentage. However, this premium seems to have narrowed in light of increased risk appetite of investors and NTPC's track record of capacity addition. Although NTPC's operating cash flows and investments would be sufficient to fund its capex plans, the strong balance sheet does not necessarily translate into speedy completion of projects.

In our Q3FY10 Result Update dated Feb 05, 2010, we had stated "We expect the stock to trade in the Rs. 188 – Rs. 225 price band for the next 2-3 months. Investors wishing to add defensive stocks to their portfolio could add NTPC on declines to Rs. 185-190." Thereafter, the stock touched a low of Rs. 196.10 (Feb 06) and a high of Rs. 212.20 (Apr 09). Despite disappointing capacity additions, due to its relatively riskfree model (a virtue in times of risk aversion), we maintain the same recommendation for the next quarter.

## Financial Performance

| Particulars (Rs. cr) | FY08 | FY09 | FY10 (E) | FY10 (A) | FY11 (E) |
|---|---|---|---|---|---|
| Net Sales | 37050.1 | 41923.7 | 45863.0 | 46322.6 | 50954.5 |
| PBIDT | 14191.5 | 13720.3 | 15323.0 | 15344.5 | 16975.0 |
| PBIDTM % (excluding other income) | 30.3 | 24.8 | 26.8 | 26.8 | 27.0 |
| PAT | 7414.8 | 8201.3 | 8896.2 | 8728.2 | 9471.6 |
| EPS | 9.0 | 9.9 | 10.8 | 10.6 | 11.5 |
| Equity | 8245.5 | 8245.5 | 8245.5 | 8245.5 | 8245.5 |
| P/E | 22.4 | 20.2 | 18.6 | 19.0 | 17.5 |
| Book Value | 63.8 | 69.6 | 75.0 | 75.7 | 83.0 |

*Quick estimates

**RETAIL RESEARCH Tel: (022) 3075 3400 Fax: (022) 2496 5066 Corporate Office**
HDFC Securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066 Website: www.hdfcsec.com
Email: hdfcsecretailresearch@hdfcsec.com